US ISM Highlights That Second-Round Effects of Trade Wars Still Lie Ahead

- US ISM-manufacturing disappointed…
- ...leaning toward the theory the prior month's gain was transitory…
- ...and driven by order front-running
- Details were weak as higher production sped up inventory depletion…
- ...but new orders and hiring retreated at a quicker pace
- Industry breadth was disturbingly poor
- Construction spending also disappointed

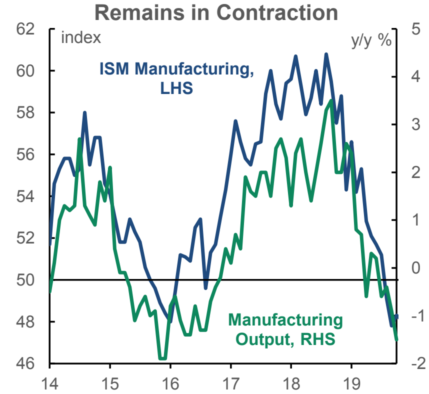
ISM manufacturing, % diffusion index, SA, November:
Actual: 48.1
Scotia: 48.8
Consensus: 49.2
Prior: 48.3

- Manufacturing continues to contract in the US as ISM disappointed expectations. Details were weak and reinforced the headline disappointment. By industry, the breadth of the weakness was widespread.
- The overall tone of the report plays to the notion that the mild improvement in ISM during October was transitory and probably geared toward front-running the mid-October threats of another layer of China tariffs and Brexit concerns, both of which got pushed out.
- Stocks sold off following the release with indices down by ¼% to ½% while the two year Treasury yield fell by only about 1bp and the USD weakened and the USD depreciated by about ¼% on a DXY basis.
- As chart 1 demonstrates, ISM-manufacturing suggests that manufacturing output continues to contract. ISM is better correlated with manufacturing output than the Markit gauge. So much for bringing manufacturing home with tariffs! Global manufacturing PMIs are mixed (chart 2).
- Details for ISM were weak as higher production and faster inventory burn were accompanied by weaker new orders and softer employment. New orders contracted at a faster pace (47.2, 49.1 prior). Inventories remain high (chart 3).
- Ditto for employment (46.6, 47.7 prior). Production still fell but at a slower pace (49.1, 46.2 prior) and this caused the order backlog to diminish at a quicker pace (43.0, 44.1 prior). Prices paid are still falling but at a slightly slower pace (46.7, 45.5 prior)
- Breadth was poor. Only 28% of industries reported overall growth which is the same as in October that in turn compared to readings in the 50–75%

CONTACTS

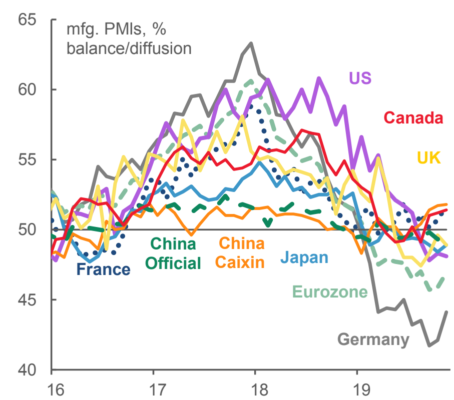
Derek Holt, VP & Head of Capital Markets Economics
416.863.7707
Scotiabank Economics
derek.holt@scotiabank.com

US Manufacturing Remains in Contraction



Sources: Scotiabank Economics, Institute for Supply Management, Federal Reserve.

Global Manufacturing



Sources: Scotiabank Economics, Markit, ISM.

U.S. Manufacturing & Trade Inventories/Sales

Source: Scotiabank Economics, U.S. Census Bureau.

range over the period up to August. Only 28% of industries report growth in new orders, 39% growth in production, 28% growth in employment and 28% growth in export orders.

- Construction spending also disappointed expectations. Spending fell by 0.8% m/m in October (+0.4% consensus) and the prior month was revised sharply lower to –0.3% m/m (+0.5% prior). Weakness across residential and nonresidential categories was widespread.